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IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 248

MEMPHIS LIGHT, GAS AND WATER DIVISION, *Petitioner*

v.

UNITED GAS PIPE LINE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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v.

UNITED GAS PIPE LINE COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

Memphis Light, Gas and Water Division ("Memphis") petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case entered January 10, 1968[1] (Appendix B to FPC Petition).

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[1] By order of this Court issued May 22, 1968, Memphis' time for filing of a petition for a writ of certiorari was extended to and including June 29, 1968.

OPINIONS BELOW

The Opinion of the Court of Appeals on remand (Appendix A to FPC Petition) is reported at 388 F.2d 385. Its order entered March 1, 1968, denying rehearing is printed as Appendix C to FPC Petition. The opinion and order of the Federal Power Commission ("Commission") are reported at 31 FPC 1180 (II R 32-55; see II R 41-42,[2] 31 FPC at 1190-1191, for the relevant portions). The Commission's decisions on the applications for rehearing are reported at 32 FPC 687, 879, and 1163. The record has been filed in support of the Commission Petition for a Writ of Certiorari.

JURISDICTION

The judgment of the Court of Appeals on remand was entered January 10, 1968 (Appendix B to FPC Petition). Memphis invokes the jurisdiction of this Court under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTIONS PRESENTED

1. Whether United Gas Pipe Line Company ("United") in its application for rehearing alleged as error the Commission's classification of United as a regulated company under the Commission's tax allocation formula as required by Section 19(a) of the Natural Gas Act so as to entitle United to judicial review of that classification under Section 19(b) of the Act.

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[2] Unless otherwise stated, the references are to the record on file with this Court in Nos. 127 and 128, Oct. Term, 1966.

2. Assuming, *arguendo*, an affirmative answer to Question No. 1, was the Commission's inclusion of United in the regulated group of companies correct as a permissible exercise of its expert judgment based on the evidence and the law.

STATUTE INVOLVED

The Natural Gas Act, June 21, 1938, c. 556, 52 Stat. 821-833, as amended, 15 U.S.C. 717-717w, provides in pertinent part:

> "Sec. 4. (d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. . . ."
>
> "(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State commission, or gas distributing company or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such

rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. . . ."

"Sec. 19 (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. *The application for rehearing shall set forth specifically the ground or grounds upon which such application is based.* Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon. . . ." (italics supplied)

"(b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole

or in part. . . . Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. *No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.* The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. . . ." (italics supplied)

STATEMENT

An aspect of this case, which involves the proper allowance for federal income taxes to be included in United's cost of service in determining just and reasonable rates for its sales of natural gas for resale in interstate commerce, was before this Court in *Federal Power Commission* v. *United Gas Pipe Line Company,* 386 U.S. 237 (1967). At that time, this Court, reversing the United States Court of Appeals for the Fifth Circuit (357 F. 2d 230), (1) upheld the Commission's power to determine United's federal income tax allowance by allocation of the actual taxes paid under a consolidated federal income tax return, in which United is one of the companies filing the return, and (2) held that the formula established and employed by the Commission to accomplish the allocation was neither "erroneous" nor "contrary to its statutory authority" (386 U.S. at 245).

Under the Commission's tax allocation formula, sustained by this Court, the companies participating in the filing of the consolidated return are first grouped

into regulated and unregulated categories.[3] After the companies are grouped in these categories, the net losses and net income of the unregulated group of companies are set off against each other. This has the effect of giving the unregulated group of companies the benefit of the tax savings made possible by the losses of the unregulated companies before the regulated group of companies share in that tax savings. When the combined losses of the unregulated group of companies exceed their combined incomes, the spillover is applied against the respective incomes of the regulated group of companies in proportion to their taxable incomes.

In this case, United, its parent United Gas Corporation, and Union Producing Company,[4] an affiliated gas and oil producer, were included by the Commission in the regulated category, although each of them, in addition to regulated business activities, is engaged in business activities which are completely free of any regulation.

The application of the formula disclosed that, over a representative period of time, United's actual tax lia-

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[3] The "regulated" category, with this Court's approval, includes companies subject to Commission jurisdiction and companies "which are regulated not by it but by state or local authorities". (386 U.S. at 246). "Regulated" and "unregulated" under the tax allocation formula are thus not necessarily synonymous with "jurisdictional", i.e., subject to Commission jurisdiction under the Natural Gas Act, and "non-jurisdictional", i.e., not subject to Commission jurisdiction.

[4] Union Producing Company is United's "producing arm". *Union Producing Co.*, 31 FPC 41, 43 (1964); *Mississippi River Fuel Corp.* v. *FPC*, 252 F. 2d 619, 622-23 (CADC 1957); *Willmut Oil and Gas Co.* v. *FPC*, 299 F. 2d 111 (CADC 1962).

bility, as a result of its participation in the consolidated tax return, equated to an effective tax rate of 50.04 percent of its taxable income—significantly less than the 52 percent tax rate United would have experienced if it had filed a separate tax return. The Commission, therefore, used the effective tax rate of 50.04 percent in determining the federal income tax allowance to be included in United's cost of service for rate-making purposes. Using this rate, the Commission allowed United $9,940,892 for federal income taxes, instead of $12,099,662 claimed by United on the basis of a 52 percent corporate tax rate which it would not actually pay, and allocated this federal income tax allowance between United's jurisdictional and non-jurisdictional business in accordance with the Commission's traditional, judicially-approved, cost allocation procedures that are unchallenged in these proceedings.

In application for rehearing to the Commission, in petition for review to the court below, and in briefs in that court, United challenged only the Commission's power to adopt and apply "to United an effective tax rate resulting from the so-called effect of the consolidated return". (R. 136-7; Exhibit "A" to Petition for Review, R. 159).

United did not challenge the Commission's inclusion of United in the regulated category in the application of the tax allocation formula until the Commission's order was before this Court.

In its brief in this Court, United for the first time contended that the Commission "wrongfully placed" United "all in" the " 'regulated' " category because the Commission "does not regulate United's intrastate business" (Brief of United, Nos. 127 and 128, Oct.

Term, 1966, pp. 30-31). Noting United's contention regarding its own classification, this Court (386 U.S. at 247) deemed "it appropriate for the issue to be raised" in the court of appeals "if the parties are so inclined".

Following issuance of this Court's judgment, United, on April 14, 1967, filed a motion in the court below for consideration and decision of its contention that the Commission erred in placing United in the regulated category and should have divided United into regulated and unregulated categories on the basis of taxable income derived from each category. The motion was opposed by the Commission and Memphis on the grounds that the issue could not be raised by United and considered by the court because it had not been raised in an application for rehearing to the Commission as required by the provisions of Sections 19(a) and (b) of the Natural Gas Act,[5] and that, in any event, the Commission properly included United in the regulated category.

The court below ruled that United's application for rehearing was "sufficiently detailed and specific to permit review by this Court" of the issue raised by United in its motion. In reaching this conclusion, the court below conceded that the "Supreme Court did not specifically pass on the question", but nevertheless, regarded this Court's remand as "a definite indication of its view" that United's contention had been preserved for court review by United as required by the

[5] Section 19(a) provides that the "application for rehearing shall set forth specifically the ground or grounds upon which such application is based". Section 19(b) provides that "No objection to the order of the Commission shall be considered by the court unless there is reasonable ground for failure so to do."

provisions of the Natural Gas Act and should be reviewed on its merits (388 F. 2d at 388).

On the merits of United's contention, the Court of Appeals ruled that the Commission, in the application of its tax allocation formula, must divide the income of a mixed company (such as United) into regulated and unregulated components, and offset all unregulated net tax losses against unregulated income (388 F. 2d at 391); otherwise, the Commission would transgress the "jurisdictional lines which Congress wrote into the Act" (388 F. 2d at 389). The court below also ruled that the Commission may only consider its own rate jurisdiction—not its certificate jurisdiction—in determining a company's appropriate classification for purposes of the tax allocation formula (388 F. 2d at 388).

Timely petitions for rehearing of Memphis and the Commission were denied by the court below on March 1, 1968.

REASONS FOR GRANTING THE WRIT

The ruling of the Court of Appeals that United, as a ground for rehearing, objected with sufficient specificity to the Commission's inclusion of United in the regulated group of companies for purposes of the tax allocation formula, and thereby preserved the issue for court review in compliance with the provisions of Sections 19(a) and (b), *supra*, p. 4, raises a question of importance in the area of judicial review of the Commission's orders and of administrative agency orders generally. Other statutes, including the Federal Power Act (16 U.S.C. 825 *l*(a) and (b)) administered by the Commission, like Section 19(b) of the Natural Gas Act, prohibit judicial consideration of alleged errors

which were not raised before the agency. *Securities Act of 1933,* Section 9(a), 15 U.S.C. 77i(a); *Securities Exchange Act of 1934,* Section 25(a), 15 U.S.C. 78y(a); *Public Utility Holding Company Act,* Section 24, 15 U.S.C. 79x; *National Labor Relations Act,* Section 10 (e), 29 U.S.C. 160(e).[6] The ruling of the court below undermines the requirements of Sections 19(a) and (b) and renders them meaningless and ineffective.

The ruling of the court below—that the Commission in the application of the tax allocation formula should have divided United's taxable income into regulated and unregulated components—is in conflict with this Court's approval of the formula, correctly described by the court below as providing for the grouping of the "*companies*" into "regulated and unregulated groups" (388 F. 2d at 388). The ruling also raises questions of substantial importance with respect to the proper role of the courts on review of the Commission's perform-

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[6] The Natural Gas and Federal Power Acts make an application for rehearing a prerequisite to court review (Sections 19(a) and 313(a)). Accordingly, they provide (Sections 19(b) and 313(b)) that court review is prohibited unless the alleged error has been brought to the Commission's attention in an *application for rehearing.* The other cited statutes do not require an application for rehearing as a prerequisite to court review. They, therefore, require that the alleged error be brought to the agency's attention *during the administrative proceeding.* This is an immaterial difference, for it is judicially established that the requirements for review are satisfied only by an "objection . . . sufficiently specific to apprise the [agency] of the question now presented." *May Stores Co.* v. *NLRB,* 326 U.S. 376, 386, note 5; *Marshall Field & Co.* v. *NLRB,* 318 U.S. 253, 255. This is the express requirement of Section 19(a) of the Natural Gas Act and of Section 313(a) of the Federal Power Act.

ance of its ratemaking responsibilities under the Natural Gas Act and Federal Power Act,[7]

In its earlier review of the orders of the Commission in this case, this Court ruled (*FPC* v. *United Gas Pipe Line Co.*, 386 U.S. 237, 244-245) that a natural gas pipeline company is not entitled to receive in rates a "hypothetical tax expense", i.e., an "expense never in fact incurred", and that it is the "duty of the Commission to limit cost of service to real expense." Yet, if the decision of the court below is permitted to stand, United's consumers, and consumers of natural gas and electric energy, generally, will be required to pay excessive rates because they will be based on "an unreal cost of service" (*FPC* v. *United Gas Pipe Line Co., supra,* at 244). In this case, the decision of the court below imposes a $12,099,662 tax allowance on consumers (computed at a 52 percent tax rate) instead of $9,940,892 (computed at the effective tax rate of 50.04 percent), thereby frustrating the primary aim of the Natural Gas Act "to protect consumers against exploitation at the hands of the natural gas companies." *FPC* v. *Hope Natural Gas Company,* 320 U.S. 591, 610 (1944).

1. A mere reading of United's assignment of error in its application for rehearing to the Commission (Exhibit "A" to Petition for Review, R. 158-9) discloses that United objected to the federal income tax allowance solely on the ground that the use of an effective tax rate, derived from United's participation in a consolidated tax return, instead of the tax rate applicable

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[7] Electric companies subject to the Federal Power Act participate in filing consolidated tax returns and are usually engaged in regulated and unregulated activities.

to a corporation filing a separate tax return, was "beyond the authority of the Commission." [8]

Conceding that "the principal force of United's argument was against the authority of the Commission to adopt a consolidated tax allocation formula", the court below nevertheless ruled that the assignment of error also challenged "the application" of the formula to

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[8] The full text of United's specification of error in its application for rehearing is as follows (Exhibit "A" to Petition for Review, R. 159-60):

> "The Commission erred in adopting and applying to United an effective tax rate resulting from the so-called effect of the consolidated return. This record shows that a consolidated effective tax rate has effect to give gas consumers the benefit of tax deductions from non-utility costs not reflected in the cost of service. Such is beyond the authority of the Commission to accomplish.
>
> "United respectfully says that the Commission further erred in directing the computation of such tax matters in connection with the decision and opinion of the Commission in *Cities Service Gas Company*, 30 FPC —, Opinion No. 396, issued July 15, 1963, in Docket No. G-18799. United shows, as the Commission of course knows, that the Cities Service Opinion is presently pending before the courts for judicial review as to the validity of such directed tax computations and the authority of the Commission so to apply them. United shows that the ultimate final judicial determination on the merits of such issues in the Cities Service case will be dispositive of the Commission's order here and United's exceptions and objections thereto.
>
> "Accordingly, United moves the Commission to supplement and amend Opinion 428 with appropriate provisions authorizing United to use and apply the statutory rate of 52% to United's separately ascertained taxable income pending final determination of the Cities Service case with appropriate provisions for refund upon the basis directed by Opinion 428 should the Commission's opinion in the Cities Service case be upheld and affirmed by the final judicial review and decision of such Cities Service case."

United as a regulated company and was therefore "sufficiently detailed and specific to permit review by this Court." (388 F. 2d at 388.)

For this strained conclusion, the court below leaned on United's use of the word "applying" in the assignment of error and its view that this Court's remand of the case for further proceedings was a "definite indication of" this Court's "view" that the issue was open for court review, although acknowledging that this Court "did not specifically pass on the question." (388 F. 2d at 383). In using the word "applying", contrary to the assumption of the Court of Appeals, United was not thereby objecting to the application of the formula to United as a regulated company. United was objecting only that the Commission had acted beyond its authority in "adopting and applying to United" an effective tax rate of 50.04 percent rather than the 52 percent corporate tax rate in computing United's federal income tax allowance (Exhibit "A" to Petition for Review, R. 159). The power of the Commission to adopt a tax allocotion formula was the *sole* focus of United's objection, not merely the "principal force" of the specification of error, as the court below would have it. Neither in general terms nor with the required specificity of Section 19(a) did United's assignment of error remotely apprise the Commission that United was challenging its inclusion in the regulated category of companies. There was no reference in the assignment of error to United's business activities and there was no claim that United must be divided into regulated and unregulated components. Indeed, the only reference to a business activity was to Union's "tax deductions from non-utility costs" to support United's claim that it was "beyond the authority of the Commission"

to "give gas consumers the benefit" of these tax deductions by using "an effective tax rate resulting from the so-called effect of the consolidated return." (Exhibit "A" to Petition for Review, R. 159), a contention expressly rejected by this Court (386 U.S. at 243-244).

Petitioner's reading of United's assignment of error finds substantial support in the fact that in extensive main and reply briefs filed by United in the Court of Appeals on the first review of the Commission's orders in this case, United neither argued nor even hinted that United was erroneously classified by the Commission under the formula. In accord with its assignment of error, in application for rehearing (Exhibit "A" to Petition for Review, R. 159-60) and in petition for review (R. 136-7), United devoted its entire argument to the proposition that the Commission's approach to the tax allowance was beyond its power and transgressed the jurisdictional limits imposed upon the Commission by Congress in the Natural Gas Act. It is not likely that United would have remained silent on the question of classification if, in fact, it had been assigned as error.[9]

The court below also erred in regarding the remand for further proceedings as "a definite indication" by this Court "of its view" that the issue of United's classification had been preserved for judicial review. Although conceding that this Court did not pass on the

[9] Even in its brief opposing the petitions for writs of certiorari (Nos. 1301 and 1302, Oct. Term, 1965), United argued only that the Commission's effective tax rate approach was beyond its authority. Apparently, by the time United came to its brief on the merits, following the granting of certiorari, United's confidence in its position must have been shaken, for the untimely assignment of error on brief was an obvious effort to hedge its position.

procedural question (388 F. 2d at 388), the court below found it "difficult to believe that the Supreme Court would have remanded this case to us for further proceedings if the Commission and Memphis are correct in their opposition to the motion on this ground" (388 F. 2d at 388).

There is no difficulty, however, about a remand for further proceedings even where judicial review of the issue may be foreclosed. On remand, the further proceedings would include, as in fact they did in this case, consideration first of the right to judicial review and then, if the right to review were sustained, consideration of the merits of the substantive issue.

On the facts of this case, there is no basis for the lower court's conclusion that this Court's remand indicated a view that the substantive issue had been properly preserved for judicial review. The procedural question was not presented, briefed, or argued to this Court in the earlier round. United's application for rehearing was not printed and the assignment of error here involved received no attention. In stating that it was "appropriate for the issue to be raised" in the court below "if the parties are so inclined" (386 U.S. at 247), this Court, we submit, was expressing no view either on the availability of the issue for judicial review or on the merits of the issue.[10]

The requirements of Section 19(a) are not merely technical, as the court below appears to have believed

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[10] The court below also regarded the remand as indicating this Court's feeling that United's contention, with respect to its classification for purposes of the tax allocation formula, had merit (388 F. 2d at 389). It is abundantly clear, however, that this Court refrained from expressing a view on the issue "to which the Court of Appeals has not addressed itself" (386 U.S. at 247).

(388 F. 2d at 388). This Court has emphasized in passing on the Section 19 requirements that "... orderly procedure and good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts." *FPC* v. *Colorado Interstate Gas Co.*, 348 U.S. 492, 500. The requirement has been rigorously enforced by the courts. *Ibid.*; *Wisconsin* v. *FPC*, 373 U.S. 294, 307.

This Court in *Colorado Interstate*, in language that is particularly appropriate to the circumstances of this case, said (348 U.S. at 501)—

> "The necessity for prior administrative consideration of an issue is apparent where, as here, its decision calls for the application of technical knowledge and experience not usually possessed by judges. The Federal Power Commission is a legislative agency the decisions of which involve these difficult problems of policy, accounting, economics and special knowledge that go into public utility rate making. For reviewing a rate made by the Federal Power Commission, the Court of Appeals has no inherent suitability comparable to that which it has for reviewing the judicial decisions made by a United States District Court." [11]

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[11] In *Colorado Interstate*, the natural gas pipeline company objected in its application for rehearing to an allocation method as not proper, but on review it claimed that its objection went to the validity of a merger condition which required the allocation. The Supreme Court ruled that the objection did not meet the Section 19 requirements in that it gave the Commission no notice that the company was attacking the validity of the merger condition. Here, United objected only to the Commission's power to adopt a tax allocation formula. It gave no notice to the Commission that its inclusion of United in the regulated category was under attack and afforded the Commission no opportunity to deal with the attack.

2. Assuming, *arguendo,* that judicial review was not foreclosed, the court of appeals erred in ruling that the Commission in computing United's federal income tax allowance under the tax formula must divide United into regulated and unregulated categories on the basis of its taxable income from each category, to avoid transgression of the Congressional limitation of the Commission's jurisdiction to interstate sales and transportation of natural gas under the Act (388 F. 2d at 389).

The court of appeals' ruling imposes a modification of the formula that is not required and conflicts with this Court's approval of the formula in *FPC* v. *United Gas Pipe Line Company, supra.* This Court has held that the tax formula, which provides for classification of the *companies*[12]—the tax paying entities—into regulated and unregulated groups, does "not exceed the powers granted to it by Congress" (386 U.S. at 243), and does not offend the requirement for separation of costs between jurisdictional and non-jurisdictional business (386 U.S. at 244-245). Referring specifically to United, this Court held that the Commission did *not* violate "the rule that the income and expense of regulated and unregulated activities should be segregated" in "arriving at the net taxable income of United" or *"in determining the tax allowance"* (386 U.S. at 243; italics supplied).

The court of appeals erred because it did not understand the function of the Commission's tax allocation formula. Its function is to apportion an equitable share of the consolidated tax among the regulated and unregulated businesses. After this apportionment the

[12] Under the ruling of the court of appeals, United's tax liability on its jurisdictional and non-jurisdictional pipeline business would be computed at different rates, a result at war with fact and reality.

allocation of that share between jurisdictional and nonjurisdictional business of the company takes place as a separate step.

Having determined United's share of the consolidated tax, the Commission, as it did with respect to all of United's total costs of service, allocated the tax and other costs of United between jurisdictional and nonjurisdictional business in accordance with its traditional allocation procedures which have received judicial sanction (388 F. 2d at 389). There was, therefore, no violation by the Commission of the Act's jurisdictional limitations in the computation of United's tax liability. The Commission recognized and took account of the fact "that United has both jurisdictional and nonjurisdictional activities and income." (386 U.S. at 247).

The ruling of the court below was also based on a misunderstanding of the Commission's decision in the *Cities Service Gas Company* case, 30 FPC 158, in which the formula, as approved by this Court, was conceived and applied. To determine "whether there is merit in United's contention", the court of appeals looked "to the commission's *Cities Service* decision itself. . ." (388 F. 2d at 389). Looking to the *Cities Service* decision, the court found that the formula was applied to the pipeline company whose rates were there being determined, Cities Service Gas Company, in precisely the same way that it was applied to United, the pipeline company in this case. Cities Service Gas Company was included in the regulated group of companies, although like United, it was only partially regulated by the Commission and made substantial sales of natural gas which were not regulated by the Commission or by state or local authorities (30 FPC at 181). On the court's own premise, therefore, the Commission's appli-

cation of the formula to United should have been affirmed.

But the court sought to distinguish the cases on the ground that Cities Service Gas Company was not divided "into regulated and unregulated components" because it had presented no evidence upon which such an allocation could be made, whereas "there is ample evidence of record in the present case by which an allocation may be made and a separation of the regulated and unregulated components of United calculated" (388 F. 2d at 391).

For this distinction, which does not exist, the court below relied on the following statement in the Commission's *Cities Service* opinion: "Cities Service . . . failed to present any evidence upon which to make such an allocation." (30 FPC at 163). But this statement, contrary to the assumption of the court below, did not refer to evidence upon which an allocation of Cities Service Gas Company itself could be made. The Commission was referring to the failure of Cities Service Gas Company to present such evidence for two oil and gas producing affiliates, Cities Service Oil Company and Cities Service Production Company (30 FPC at 163).

The fact is that the record in the *Cities Service* case, *supra,* as does the record in every rate proceeding in which a natural gas pipeline company's rates are being fixed, contained the same type of data respecting Cities Service Gas Company that the court of appeals deemed sufficient to divide United into regulated and unregulated activities and income. And on the basis of such data, the Commission separated Cities Service Gas Company's total cost of service, including its share of the consolidated tax liability, between jurisdictional and non-jurisdictional business.

Finally, the court of appeals exceeded its "essentially narrow and circumscribed" review authority in failing to sustain the Commission's inclusion of United in the regulated group of companies on the basis of its finding (II R 41) that "United is largely a regulated company" and should be designated "as such for the purpose of these (tax) computations" (material in parenthesis supplied). The finding was supported by substantial evidence and represented an informed judgment in an area in which the Commission has expertise. *Permian Basin Area Rate Cases,* U.S. , 36 LW 4337, 4341 (1968); *Hardin* v. *Kentucky Utilities Co.,* U.S. , 36 LW 4134, 4136 (1968); *Colorado Interstate Gas Co.* v. *FPC,* 324 U.S. 581, 589 (1945); *FPC* v. *Hope Natural Gas Co.,* 320 U.S. 591, 602 (1944).

The evidence disclosed that at least 54.44 percent of United's revenues are derived from sales of natural gas which are subject to rate regulation by the Commission and other authorities. An additional portion of United's revenues are derived from sales which involve the use of facilities that are certificated by the Commission because the sales involve transportation of natural gas in interstate commerce, although the rates at which such sales are made are not regulated by the Commission.

The court below ruled that the Commission may not consider its certificate jurisdiction in separating companies under the formula into regulated and non regulated categories. (388 F. 2d at 388.)

The Commission's finding was supported by the 54.44 percent of regulated revenues alone. Additionally, however, the ruling of the court below on certificate jurisdiction is erroneous and runs afoul of this Court's decision in *FPC* v. *United Gas Pipe Line Co., supra.*

As used in the formula, a "regulated" company may be a company which is regulated only "by state or local authorities" (386 U.S. at 246), and as so construed, the formula was approved by this Court.

Since the Commission may rely on regulation by State and local authorities to include a company in the regulated category—even where there may be no Commission rate regulation of that company at all—the ruling of the court below conflicts with this Court's approval of the formula and is neither rational nor logical. Moreover, the investment in, and operating costs of, certificated facilities from which non-FPC regulated sales are made, have a distinct relationship to the Commission's rate jurisdiction. They affect and enter into the cost of service, and ultimately the rates, that are subject to Commission jurisdiction.[13]

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[13] For this reason, applications for authority to construct and operate facilities for the transportation of natural gas in interstate commerce, whether or not the sales from such facilities are subject to Commission jurisdiction, are required to include data showing the effect on systemwide operating revenues and expenses of the estimated revenues and expenses related to the proposed facilities. *FPC Regulations Under the Natural Gas Act, Section 157.14(16)*. When the proposed facilities will result in a material change in the applicant's average cost of service, the applicant must also present a cost of service for the system reflecting the operation of the proposed facilities together with an allocation of such costs to each particular service classification. *Id., Section 157.14(18)(ii)(a) and (b)*. Cf. *Panhandle Eastern Pipe Line Co.* v. *FPC*, 324 U.S. 635, 646-647 (1945), in which this Court, citing Section 5(a) of the Act, held that the "Commission, while it lacks authority to fix rates for direct industrial sales, may take those rates into consideration when it fixes rates for interstate wholesale sales which are subject to its jurisdiction" in order that the Commission may assure that the business subject to its jurisdiction is not being saddled with costs that should be borne by the unregulated business.

The mistakes made by the court of appeals in this case emphasize the wisdom of the requirement of the Natural Gas Act that alleged errors must first be presented to the Commission.

CONCLUSION

This petition for a writ of certiorari should be granted and the judgment of the court below reversed without further briefs or argument since the decision of the court below is so clearly contrary to, and in conflict with, the evidence and decisions of this Court on the questions presented.

Respectfully submitted,

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